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August 31, 2005

Mary L. Cottrell, Secretary  
Department of Telecommunications and Energy  
One South Station  
Boston, MA 02110

Re: Bay State Gas Company, D.T.E. 05-27

Dear Secretary Cottrell:

Enclosed for filing please find the Initial Brief of KeySpan Energy Delivery New England in the above-referenced case.

Thank you for your attention to this matter.

Very truly yours,



Robert J. Keegan

Encl.

cc: Caroline Bulger, Hearing Officer  
Andrew Kaplan, General Counsel  
John Cope-Flanagan, Assistant General Counsel  
George Yiankos, Director, Gas Division  
Robert Dewees, Esq.  
Service List

**COMMONWEALTH OF MASSACHUSETTS**  
**DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY**

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D.T.E. 05-27

**INITIAL BRIEF OF**  
**BOSTON GAS COMPANY d/b/a**  
**KEYSPAN ENERGY DELIVERY NEW ENGLAND**

Submitted by:

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Dated: August 31, 2005

**COMMONWEALTH OF MASSACHUSETTS**  
**DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY**

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Bay State Gas Company

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**INITIAL BRIEF OF**  
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**I. INTRODUCTION**

In this proceeding, the Department of Telecommunications and Energy (the “Department”) is reviewing a request by Bay State Gas Company (“Bay State”) for approval of a Performance-Based Rate Plan and other rate adjustments under G.L. c. 164, § 94. Bay State’s request was filed on April 27, 2005 and docketed by the Department as Bay State Gas Company, D.T.E. 05-27. On June 2, 2005, the Department granted intervenor status in this proceeding to Boston Gas Company d/b/a KeySpan Energy Delivery New England (“KeySpan” or the “Company”). On July 8, 2005, KeySpan submitted pre-filed testimony on the issue of gas-cost related bad-debt recovery, recommending that the Department approve Bay State’s request to continue to recover gas-cost related bad debt expense on a reconciling basis through the Cost of Gas Adjustment (“CGA”) factor. On August 3, 2005, Joseph F. Bodanza, Senior Vice President of Regulatory Affairs and Asset Optimization for KeySpan Corporation testified at an evidentiary hearing conducted by the Department at its offices. In this Initial Brief, the Company reviews the basis for its recommendation and responds to a

briefing question posed by the Department regarding the applicability of the Department's rulings in this case to KeySpan.<sup>1</sup>

## II. BACKGROUND

### A. Operation of Traditional Bad-Debt Recovery Mechanisms

In this proceeding, Bay State is proposing to continue to recover its gas-cost related bad debts through the CGA. Exh. BSG/JES-1, at 26. The methodology Bay State has been using, and proposes to continue to use, is as follows: First, consistent with Department precedent, Bay State proposes to establish a test-year bad-debt ratio for use in projecting gas-cost related bad-debt expense in their seasonal CGA filings. Id. To do this, Bay State calculated net writeoffs (gross bad-debt write-offs less amounts collected that were previously written off) and firm billed revenues for each year of the most recent three years of operation (in this case, 2002, 2003 and 2004). Id. Bay State then computed the bad-debt ratio by dividing total net writeoffs by total firm revenues for the three-year time period. Id. Based on the historical data for 2002, 2003 and 2004, the resulting ratio of bad debts to total firm revenues is 2.17 percent. Id. at Schedule JES-6, at 9.

As stated in Bay State's proposed CGA tariff, Bay State currently includes a factor to recover gas-cost related bad-debt expense in its seasonal CGA filing. Exh. KED-1, at 3; see, Schedule JLH-1-7, § 15.00 et seq. The seasonal CGA filings are based on forecasted amounts, with the forecast of bad-debt expense calculated by multiplying

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<sup>1</sup> To respond to a request from the Department, the Company will address the applicability of the ruling in this case to KeySpan in Section IV, infra. However, in short, KeySpan is not requesting that the Department decide the issue of bad-debt recovery for Boston Gas in this case. The Company acknowledges that it will need to make a separate filing to implement a KeySpan-specific proposal for gas-related bad-debt recovery with appropriate notice and process.

the bad-debt ratio of 2.17 percent (established in this rate case) by the total projected gas costs for the upcoming season. Id. at 4; see, Schedule JES-6, at 9.

On an annual basis, Bay State reconciles the gas-cost related bad-debt amounts collected through the CGA during the previous 12-month period to its actual gas-cost bad-debt expense. Id. For reconciliation purposes, Bay State derives the gas-related bad-debt revenues collected through the CGA by multiplying the actual monthly sales by the bad-debt component approved in the initial CGA filing. See, Schedule JLH-1-7, § 15.03. Actual bad-debt expense is derived by “tracking” the actual net writeoffs associated with gas-cost collections in each month. Id.; Exh. KED-1, at 4-5. The difference between (a) the product of actual monthly sales times the approved bad-debt component, and (b) the actual monthly net writeoffs associated with gas-cost collections, represents the over-or under-collection owed to/from customers for gas-cost related bad-debt expense. Id. Bay State determines the amount of actual net writeoffs associated with gas-cost collections by applying the current ratio of annual firm gas-cost revenues to total firm revenues, to the monthly actual net writeoffs. Exh. KED-1, at 5.

The Bay State approach is virtually identical in concept to the mechanism that was in place for KeySpan prior to the D.T.E. 03-40 proceeding. Exh. KED-1, at 5. Specifically, in its seasonal CGA filings, KeySpan would project gas-cost related bad-debt expense by first calculating a bad-debt ratio, which was derived by dividing total net writeoffs for the current year by total firm revenues. Id. The Company then multiplied projected firm revenues by the bad-debt ratio to derive its projected bad-debt expense. In D.P.U. 96-50, the Department found that 62 percent of the test-year bad-debt expense was attributable to gas costs. D.P.U. 96-50, at 72. Therefore, in its seasonal CGA filings,

the Company designed the CGA rate to recover 62 percent of its projected bad-debt expense through the CGA. Exh. KED-1, at 5.

On an annual basis, KeySpan would reconcile the gas-cost related bad-debt amounts recovered through the CGA (based on projections) to its actual gas-cost related bad-debt expense experienced in the prior twelve months. Id. at 6. For reconciliation purposes, the Company derived the gas-cost related bad-debt revenue billed through the CGA by multiplying the actual monthly sales volumes by the bad-debt component approved in the initial CGA filing. Id. Actual gas-related bad-debt expense was derived by multiplying the Company's actual monthly net writeoffs by 62 percent. Id. The difference between (a) the product of actual monthly sales times the approved bad-debt component, and (b) the product of actual monthly net writeoffs times 62 percent, represented the over- or under-recovery from customers for gas-cost related bad-debt expense. Id.

Thus, there were three common elements underlying the bad-debt expense computation for Bay State and KeySpan. First, both the Bay State and former KeySpan methodologies identify a *bad-debt ratio*, which is the ratio of net writeoffs to firm revenues. Id. at 6. It is the Department's practice to establish a bad-debt ratio in a base-rate proceeding by using the three most recent years of data for total net writeoffs (gross writeoffs less amounts collected that were previously written off) and total firm revenues. See, e.g., D.T.E. 03-40, at 265. This bad-debt ratio is traditionally used in a base-rate proceeding to establish the allowed bad-debt expense associated with distribution revenues to be recovered through base rates (this amount is therefore fixed until base rates are reset). Id. The gas-cost related amount of bad debts targeted for recovery

through the CGA may also be established using the bad-debt ratio set in the base-rate proceeding as is the case with Bay State's mechanism. Exh. KED-1, at 4. However, under a reconciling mechanism, actual gas-cost related bad-debt recoveries are not generally determined by application of a fixed bad-debt ratio.

Second, both methodologies account for the *allocation of total bad-debt expense* between gas supply (CGA) and distribution revenues (base rates). *Id.* at 7. Because the total level of revenues associated with the gas-cost and distribution-rate portions of a customer's bill will vary based on consumption patterns, consumption levels and fluctuating gas costs, the allocation of total bad-debt expense between gas and distribution revenues is constantly changing. *Id.* Under Department precedent, the portion of bad-debt expenses associated with distribution revenues is included in base rates set in a base-rate proceeding and is generally not modified unless a subsequent base-rate proceeding is conducted. See, e.g., D.T.E. 03-40, at 264-265.

Under the Bay State method, the gas-cost portion of total bad-debt expense is derived by applying the current ratio of annual firm gas-cost revenues to total firm revenues, to the monthly actual net writeoffs. Exh. KED-1, at 7. For KeySpan, the Department determined in D.P.U. 96-50 that 62 percent of bad-debt expense in the test year was attributable to gas revenues. *Id.* As a result, until the Department modified its approach in D.T.E. 03-40, the Company recovered 62 percent of its actual total bad-debt expense through the CGA and 38 percent of its test-year bad-debt expense through base rates. *Id.* Since D.T.E. 03-40, the Company has the capability to track the ratio of gas-cost bad-debt writeoffs to total writeoffs using its Customer Related Information System ("CRIS"), rather than using the ratio of gas-cost revenues to base revenues or an

allocation established by the Department. Id.; See D.T.E. 03-40 (RR-DTE-94; Tr. 24 at 3299).

The third key element of the bad-debt expense computation is the *total revenue amount upon which the computation is based*. Exh KED-1, at 8. The Company's total revenues are composed of revenue billed through both distribution rates and the CGA factor. Id. Since the 2000/01 heating season, the Company and its customers have experienced a high degree of volatility in gas commodity prices, which means that the Company's total revenues and gas-cost revenues are subject to constant change. Id.

B. Operation of Bad-Debt Recovery Mechanism Under the Department's Revised Policy

In D.T.E. 03-40, the Department made fundamental changes relating to the bad-debt expense calculation for KeySpan. First, the Department established a bad-debt ratio of 1.52 percent (calculated on the basis of only two years of historical net writeoffs to total firm revenues) and applied this ratio to test-year firm revenues to fix the *total* amount of "allowed bad-debt expense" to be recovered annually until the next base-rate proceeding. D.T.E. 03-40, at 265-267. Previously, the bad-debt ratio established in the rate case was applied only to identify the test-year level of bad-debt expense for purposes of setting the amount of bad-debt expense to be recovered through distribution rates. The bad-debt ratio subsequently used in computing the gas-cost related bad-debt expense for the seasonal CGA filings would be updated so that the most recent data regarding the ratio of bad-debt writeoffs to total revenues would be incorporated into the calculation. Exh. KED-1, at 9. Updating the bad-debt ratio as part of the recovery of actual gas-cost related bad-debt expense is appropriate because the ratio of bad-debt writeoffs to total



revenue typically fluctuates as (1) base and gas revenues fluctuate, and (2) increased revenue levels translate into greater levels of customer arrearages.

A second change made by the Department relates to the allocation of bad-debt expense between the CGA and base rates. Unlike D.T.E. 96-50, where the Department fixed the allocation of bad-debt expense between base rates and the CGA on a going-forward basis at the test-year percentage for gas costs (i.e., 62 percent), the Department directed the Company to develop a program for CRIS to track the ratio of actual writeoffs relating to gas costs in each period. D.T.E. 03-40, at 266-267 (see RR-DTE-94; Tr. 24, at 3298-99). Thus, in each seasonal CGA filing, gas-cost related bad-debt expense will be projected based on the ratio of actual gas-cost related writeoffs to total writeoffs in the prior 12 months. Exh. KED-1, at 9. In the Company's experience, this modification to the policy set in D.P.U. 96-50 is reasonable and appropriate because the ratio of gas costs to total revenues fluctuates continually and fixing the allocation percentage based on the test-year ratio has the potential to lead to a mismatch between allowable bad-debt recoveries through the CGA and actual gas-cost related bad debt expense as gas costs fluctuate. By setting recoveries through the CGA based on actual gas-cost related bad-debt writeoffs, bad-debt recovery will be directly correlated to actual gas-related bad-debt writeoffs, which is a fair and reasonable approach for customers and the Company. See, Tr. 19, at 3071.

Third, and most significantly, the Department directed the Company to allocate total bad-debt expense to the CGA by applying the updated gas-cost related bad-debt writeoff ratio *to the total bad-debt expense approved in the rate case*. D.T.E. 03-40, at 267. The "allowed bad-debt expense" calculated in D.T.E. 03-40 was derived by

applying the bad-debt ratio of 1.52 percent to test-year normalized firm sales revenues to derive a total “allowed” bad-debt expense of \$9,326,004. *Id.* at 267 (Compliance Filing Exhibit KEDNE-1, at page 22 of 41). Based on the gas-to-base revenue allocation percentage of 55.3 percent determined in D.T.E. 03-40, the Department calculated gas-cost related bad-debt expense for the test year to be \$5,157,280 (or 55.3 percent of \$9,326,004). *Id.* at 267. Therefore, under the terms of the Department’s order in D.T.E. 03-40, the amount of gas-cost related bad-debt expense recovered through the CGA is allowed to vary from the test-year level of \$5,157,280 *only* to the extent that an updated ratio of actual gas-related bad-debt writeoffs to total bad-debt writeoffs will be multiplied by the “allowed bad-debt expense” of \$9,326,004. Exh. KED-1, at 10.

These changes have had significant financial ramifications for KeySpan and will have similar ramifications for Bay State and other local gas distribution companies because it is now the Department’s policy to establish the total level of bad-debt expense based on the *test-year level of revenues*, despite the fact that gas costs continue to exhibit unprecedented volatility making it difficult, if not impossible, to set a “representative” amount of gas-related bad-debt expense in rates. Because of the extreme level of volatility in gas prices, test-year bad-debt expense is not representative of the actual gas-related bad-debt expense incurred by Boston Gas since D.T.E. 03-40. Accordingly, the Department’s decision to eliminate the reconciliation of gas-cost related bad-debt expense and to limit recovery through the CGA based on (1) a fixed bad-debt ratio (1.52 percent for KeySpan); and (2) a total bad-debt expense based on test-year firm revenues (\$9,326,004 for KeySpan), is unworkable in light of the extreme volatility in gas costs.

### III. ARGUMENT

In this proceeding, the Department should approve Bay State's proposal to continue recovering gas-cost related bad debt expense on a reconciling basis through the CGA. The Department should approve this proposal for the following reasons:

First, the decision made by the Department in Fitchburg Gas and Electric Light Company, D.T.E. 02-24/25 (2002) to eliminate the reconciliation of gas-cost related bad debt runs directly contrary to the Department's findings in D.P.U. 96-50 that gas-related bad-debt expense should be reconciled when there is an expectation that variation in actual gas-related bad-debt costs will occur, therefore making it difficult to set a "reasonable" or representative amount in rates. D.P.U. 96-50, at 72; discussed in Fitchburg Gas and Electric Light Company, D.T.E. 02-24/25, at 171-172.

In D.P.U. 96-50, the Department recognized that, going forward, there was the potential for fluctuations to occur in the level of bad-debt expense incurred by gas companies because of the changes that could result from customer migration to competitive supply following the base-rate case. D.P.U. 96-50, at 72. Therefore, rather than locking in an amount in base rates to recover total bad-debt expense, the Department moved the portion of bad-debt expense relating to gas costs into the CGA, which is the mechanism designed to recover gas-related costs on a reconciling basis. In D.T.E. 02-24/25, the Department explicitly stated that, in moving gas-related bad-debt expense to the CGA, it anticipated that bad debt expense would *decrease* and its "intent" was to avoid the "recovery of bad debt expense greater than the level determined to be reasonable in a rate case." D.T.E. 02-24/25, at 171.

Regardless of the specific reasons cited in D.T.E. 96-50 for anticipated (post-rate case) changes in actual gas-cost related bad-debt expense, the Department's decision to reconcile those costs fundamentally recognized that there were factors (outside the control of the Company) that would cause volatility in the actual level of gas-related costs that the Company would incur and that, without reconciliation, there was a chance that the Company would recover bad-debt expense in an amount greater than the "reasonable" or representative level set in the rate case. The Department's decision to reconcile gas-cost related bad debt in order to address the anticipated volatility in actual costs and avoid an over-collection situation is a sound and established ratemaking strategy. However, sound ratemaking policy requires that the mechanism be applied regardless of whether circumstances cause gas-cost related bad debts to increase or decrease.

In fact, since D.P.U. 96-50, gas-related bad-debt expense has fluctuated (and increased) significantly for factors other than the customer-migration issue identified by the Department in D.P.U. 96-50. As the Department is acutely aware, gas prices have experienced more volatility and have risen more dramatically in the past five years than in the 15 years preceding the winters of 1998-99 and 1999-2000. Request for Increase in the Cost of Gas Adjustment Factors, D.T.E. 01-09, at 1 (2001).

The record shows that, in the test year for D.T.E. 03-40 (FY2002), KeySpan had total firm revenues of approximately \$610.8 million with gas costs totaling approximately \$317.6 million or roughly 52 percent. See, RR-DTE-132. In FY 2005, the Company projects that total firm revenues will be approximately \$1.05 billion with gas costs projected to total \$690.6 million, or about 65.8 percent. Exh. KED-1, at 19. As these amounts indicate, the Company's gas costs have more than doubled (increasing by \$373

million) in just three years. Although gas-cost related bad debt expense is growing in parallel, with gas-cost related bad-debt expense projected to be approximately \$15 million in 2005, the Company's allowed recovery of gas-cost related bad-debt expense under DTE 03-40 is approximately \$5 million based on test-year revenues for 2002. Exh. KED-1, at 19. The Department's decision in the Fitchburg and Keyspan rate cases to revise its policy from reconciling gas-cost related bad-debt expense to a policy of locking in both the bad-debt ratio and the amount of gas-cost related bad-debt expense based on test-year revenues has decoupled bad-debt expense from the gas-cost revenues that drive the expense level and has caused the Company to absorb substantial losses in an area where it has no ability to control gas prices and limited ability to control the related bad-debt writeoffs.

The financial impact of this policy change on Boston Gas (and on Bay State if its proposal is not approved by the Department) is substantial and, as gas prices continue to fluctuate, this policy will force base-rate proceedings, even for companies operating under PBR. Conversely, bad-debt expense amounts set in a test year where gas costs may be substantially higher than will be experienced in the future, will produce the precise result the Department intended to avoid when it initially adopted the policy of reconciling gas-cost related bad debts through the CGA in that it will potentially lock in an amount that is substantially greater than may be "reasonable" or representative in the future. The Department established the CGA with the express recognition that the periodic resetting of non-reconciling base rates simply does not work effectively or adequately for expense categories characterized by an abnormal level of volatility. See Worcester Gas Light Company, 9 P.U.R. 3d 152, 155-56 (1955). Because the level of

gas-cost related bad-debt expense is a direct function of gas costs, it is impossible to identify a representative amount of gas-cost related bad-debt expense where gas prices continue to rise and/or exhibit a high degree of volatility. Therefore, the Department should continue to allow for the recovery of gas-cost related bad debt on a reconciling basis through the CGA.

A second consideration involved in the Department's decision to eliminate the reconciling mechanism for gas-related bad-debts was the concept that fixing the total allowable expense would provide an "incentive" for gas companies to reduce gas-related bad-debt expense. However, gas companies have no control over commodity prices established in the competitive marketplace, nor do gas companies have control over the consumption of gas by customers. Therefore, to the extent that gas costs are a function of market prices and customer consumption, gas companies have no control over gas costs or their impact on total firm revenues and associated bad debts. Moreover, it is always in a company's interest to collect revenues that are owed by the customer, whether the revenues are currently owed, are overdue, or have previously been written off. Under a PBR mechanism, the gas companies are under extreme pressure to control the costs associated with bad debts and to make every effort to collect overdue amounts from customers. In doing so, the gas companies make no distinction between gas-cost related bad debt and distribution-related bad debt. See, Tr. 19 at 3076-77. Thus, the elimination of the reconciliation of gas-cost bad-debt expense does not create the "incentive" sought by the Department in reversing its ratemaking policy. Rather, the reversal of ratemaking policy simply undermines the financial operations of the LDC and will require more

frequent base-rate adjustments regardless of whether a company is operating under a PBR plan.

In that regard, the record in this proceeding shows that the bad-debt recovery mechanism adopted by the Department in D.T.E. 03-40 (and D.T.E. 02-24/25) has resulted in substantial under-recoveries of gas-cost related bad-debt expense. RR-DTE-131. In the response to RR-DTE-131, KeySpan analyzed the impact of applying the Department's methodology in D.T.E. 03-40 (which fixed the total allowed bad-debt expense at the test-year level) versus the D.P.U. 96-50 methodology (which fixed the allocation percentage but allowed the expense level to vary) and Bay State's existing reconciliation method (which allows recovery of actual gas-cost writeoffs). This analysis shows that, with total bad-debt writeoffs of \$114,056,848 over an 8-year period and applying the percentages approved in D.T.E. 03-40, the D.T.E. 03-40 method would have resulted in total bad-debt recoveries of \$77,527,073; the D.P.U. 96-50 method would have resulted in recoveries of \$96,423,229 and the Bay State methodology would have resulted in recoveries of \$103,544,708. Thus, *none* of the mechanisms result in "dollar for dollar" recovery of the actual bad-debt writeoffs of \$114,056,848; however, the D.T.E. 03-40 method would produce under-recoveries of \$36,529,775 (or 32 percent) versus the under-recovery produced by the Bay State methodology of \$10,512,140 (or 9 percent). Accordingly, the Bay State methodology produces an equitable result that more closely tracks gas-cost related bad debt expense over time.

Therefore, in this proceeding, the Department should maintain Bay State's existing methodology for computing and recovering gas-cost related bad-debt expense because the variation in gas-cost related bad-debt expense is substantial and is directly

correlated to the increase in gas costs. In fact, continuation of Bay State's existing bad-debt recovery mechanism is necessary in view of: (1) the Department's previous policy decision to establish the CGA to recover gas-related costs, (2) the Department's previous policy decision to move gas-related bad debt expense to the CGA for recovery in light of anticipated cost changes that would make it difficult to set a representative level of gas-cost related bad-debt expense: (3) the companies' lack of control over volatile gas prices and related gas-cost related bad debts, and (4) the serious, negative financial impacts associated with applying a non-reconciling cost recovery mechanism for gas-cost related bad debts, especially during a ten-year PBR plan.

#### **IV. APPLICABILITY TO KEYSpan**

In this proceeding, Bay State is proposing to maintain its existing mechanism for recovering gas-cost related bad-debt expense, which allows for the recovery of actual gas-related bad-debt writeoffs on a reconciling basis. The Department's approval of this proposal would signify the re-establishment of its traditional ratemaking policy allowing the recovery of actual gas-cost related bad debts on a reconciling basis. In D.T.E. 03 40, the Department referenced its intent in the earlier Fitchburg decision (D.T.E. 02-24/25) to signal a policy change regarding bad-debt recoveries, which was then applied in the KeySpan case without any additional investigation or inquiry.<sup>2</sup> Similarly, the Department's approval of Bay State's proposal in this case would signal a policy change

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<sup>2</sup> It is well established that the Department has the authority to establish policy in company-specific cases that can then be applied to other companies within its jurisdiction when those companies come before the Department. See, Tr. 19 at 3063 ("the companies are responsible for knowing what's in each and every order we issue"); See also, D.T.E. 03-40, Tr. 24, at 3298-3300 (Department staff questioning the KeySpan witness as to the bad-debt holdings in D.T.E. 02-24/25 regarding gas-cost related bad debt).



applicable to all gas companies, but the implementation of that policy in this case would apply only to Bay State's rates, which are the subject of this adjudicatory proceeding.

However, this is not to say that KeySpan would require a base-rate proceeding to apply the Department's policy decision. In D.T.E. 03-40, the Department computed a bad-debt ratio of total net writeoffs (gross writeoffs less amounts collected that were previously written off) to total firm revenues. See, D.T.E. 03-40, at 265. Based on the ratio of gas revenues to total revenues, the Department then established the amount of bad debts that would be recovered through base rates and the amount that is related to gas costs and would be recovered through the CGA. Id. The portion of bad-debt expense associated with distribution revenues and recovered through base rates is fixed until base rates are reset in a future base rate proceeding. *KeySpan would not be proposing to change this amount.* In a KeySpan-specific case, Boston Gas will propose only to change the amount of gas-cost related bad-debt recoveries allowed through the CGA, which is within the Department's discretion to implement. Bad-debt recoveries through the CGA are allowed to fluctuate, even under the mechanism approved in D.T.E. 03-40. Therefore, the Department's determination is one only of the *amount* of recovery to be allowed through the CGA.

Although not subject to determination in this case, there are two alternatives for KeySpan to pursue in terms of collection of under-recovered gas-cost related bad-debt expense since the Department's rate decision on October 31, 2003. First, the reconciling nature of the CGA would allow for the recovery of under-recovered gas-cost related bad debt amounts and, in fact, the Department has allowed restatements of CGA reconciliations in the past to make corrections, such as changes in tax rates occurring

after reconciliations are completed. This type of recovery would not constitute retroactive ratemaking because the limitations on retroactive ratemaking apply only to base-rate changes and do not apply to a reconciling rate mechanism. Specifically, the Supreme Judicial Court has determined that:

[W]e have no difficulty in concluding that an order retroactively adjusting a CGAC is well within the [D]epartment's general supervisory authority over utility costs, see G. L. c. 164, s. 76, and is consistent with its "broad authority to determine ratemaking matters in the public interest." Massachusetts Inst. of Tech. v. Department of Pub. Utils., 425 Mass. 440 Mass. 856, 868 (1997). [footnote omitted]. Retroactivity is inherent in the very nature of a CGAC. Unlike the base rate, which is a calculation of rates going forward based on historical data, the CGAC adjusts semiannually for utility costs as they actually have been incurred, according to a mechanically applied technical formula. See Consumers Org. for Fair Energy Equality, Inc. v. Department of Pub. Utils., *supra* at 606.

Fitchburg Gas and Electric Light Company v. Department of Telecommunications and Energy, 440 Mass. 625 (2004), at 637-638. See also Automobile Insurers Bureau of Massachusetts v. Commissioner of Insurance, 425 Mass. 262, at 268 (1997) ("the annual reconciliation process...requires that the commissioner go back for up to four years").

Secondly, KeySpan has the alternative of proposing exogenous cost recovery through its PBR mechanism. In September, the Company will make its second annual compliance filing following the D.T.E. 03-40 decision. In that filing, rate adjustments (including any exogenous cost adjustments) will be implemented for calendar year 2004. Recovery as an exogenous cost under the PBR Plan also would not constitute retroactive ratemaking because the mechanism is explicitly designed to function in this manner.

Because KeySpan plans to submit a company-specific filing proposing that the amount of gas-cost related bad debts allowed to be recovered through the CGA be reconciled based on the level of Boston Gas' actual gas-cost related bad-debt expense,

issues regarding KeySpan specific implementation would not need to be addressed in the Department's order in D.T.E. 05-27. The Department's decision in this case to approve the Bay State proposal would have the effect of setting a ratemaking policy for Massachusetts LDCs and implementing that policy in this case only for Bay State.

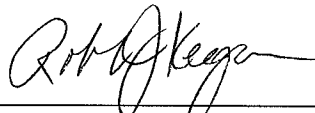
## **V. CONCLUSION**

For the foregoing reasons, the Department should approve Bay State's proposal to maintain and continue its reconciling mechanism for gas-cost related bad-debt expense. This finding would establish a policy for gas companies operating within the Commonwealth standing for the proposition that it is appropriate to recover actual gas-cost related bad debts through the CGA on a reconciling basis because these costs are a gas cost subject to the volatility of gas prices in the marketplace.

Respectfully submitted,

**Boston Gas Company d/b/a  
KeySpan Energy Delivery New England**

By its Attorneys,



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Dated: August 31, 2005